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IN THE

Supreme Court of the United States

October Term, 1958.

No. 714

MADISON FUND, INC. (Formerly The Pennroad Corppration) and AFFILIATED COMPANIES,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

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IN THE

Supreme Court of the United States.

OCTOBER TERM, 1958.

No.

MADISON FUND, INC. (FORMERLY THE PENNROAD CORPORATION) AND AFFILIATED COMPANIES,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

Madison Fund, Inc. (formerly The Pennroad Corporation),[1] and its affiliated companies, prays that a writ of certiorari issue to review the judgments of the United States Court of Appeals for the Third Circuit entered on November 26, 1958 in two cases, *viz., The Pennroad Corporation and Affiliated Companies v. Commissioner of Internal Revenue* (No. 12,597) and *The Pennroad Corporation and Affiliated Companies v. Commissioner of Internal Revenue* (No. 12,598).

1. On October 15, 1958 The Pennroad Corporation changed its name to Madison Fund, Inc. by filing a Certificate of Amendment to its Certificate of Incorporation with the Secretary of State of the State of Delaware and by recording the same on the same day.

OPINIONS BELOW.

The two cases with respect to which a writ of certiorari is here sought involve identical questions relating to the petitioner's income tax liability for the years 1950 through 1952. They were consolidated for hearing before the Tax Court, and, upon appeal, were consolidated for hearing before the Court of Appeals. The findings of fact and opinion of the Tax Court (R. 60a-84a) [2] are reported at 29 T. C. 914. The opinion of the Court of Appeals affirming the Tax Court is printed in Appendix B, *infra*, page 27 and is reported in 261 F. 2d 325.

JURISDICTION.

The judgments of the Court of Appeals, which are printed in Appendix B, *infra*, page 37, were entered on November 26, 1958. The jurisdiction of this Court is invoked under Section 1254(1) of the Judicial Code, 28 U. S. C. § 1254(1).

QUESTION PRESENTED.

A corporation invested in a large tract of real estate adjacent to the waterfront at Baltimore, Maryland. During a period of over one hundred years it improved portions of such real estate for permanent rental and developed, through subsidiary companies, substantial railroad and stevedoring businesses from which, in conjunction with real estate and equipment rentals, it now realizes almost 90% of its income. During the same period it gradually and continuously liquidated the balance of such real estate and (except in minor respects) re-invested any sales proceeds not distributed to its stockholders in depreciable assets rented to its subsidiaries or in industrial improvements to leased property. Its only purchases of additional real

2. This and similar references are to page numbers of the Appendix filed by the petitioner with the Court of Appeals.

estate were a few parcels (1) to round out portions of the original tract, and (2) for a proposed extension, later abandoned, of the right of way of its railroad subsidiary. Its advertising and business activities in connection with the liquidation were the minimum necessary to make it profitable, and did not resemble those of the usual real estate dealer.

The question is whether the corporation, by liquidating its investment in an orderly, business-like fashion and with no intent to re-invest in other real estate, must be deemed to have entered the real estate business so that gains on the sales of such real estate must be treated as ordinary income rather than capital gains.

STATUTES AND REGULATIONS INVOLVED.

In sum, the statutory provisions involved provide that where real estate is "held primarily for sale to customers in the ordinary course of [a taxpayer's] trade or business" the gains from the sale of such real estate are ordinary income.

The statutory provisions are Sections 117(a)(1), (4), (6) and (8) of the Internal Revenue Code of 1939.[3] They are printed in Appendix A, *infra*, page 23.

The Regulations involved are Treasury Regulations 111, § 29.117-1 (applicable to the taxable years 1950 and 1951), and Treasury Regulations 118, § 39.117(a)-1 (a) and (b) (applicable to the taxable year 1952). The relevant portions of the two regulations are printed in Appendix A, *infra*, page 24, and are substantially identical.

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3. The provisions of the Internal Revenue Code cited are those applicable to the taxable years here involved. There has been no substantial change in those provisions affecting the question presented by this case. Section 1237 of the Internal Revenue Code of 1954 provides for capital gains treatment in specific circumstances of real estate subdivided for sale, but that section (except in minor respects) applies only to individuals.

STATEMENT OF THE CASE.

A. Nature of the Proceeding.

This case involves the consolidated Federal income tax of the petitioner and its affiliated companies for the taxable years 1950 through 1952.

Petitioner is an investment company registered with the Securities and Exchange Commission as a closed-end management company pursuant to the Investment Company Act of 1940. As the common parent corporation of an affiliated group of companies, it filed consolidated Federal income tax returns for itself and its affiliated companies for the years in question. Among the affiliates were Canton Company of Baltimore ("Canton"), Canton Railroad Company ("Canton Railroad"), and The Cottman Company ("Cottman").

During the taxable years in question Canton sold certain parcels of real estate, and in the consolidated returns filed by the petitioner the gains from such sales were reported as capital gains. The Commissioner of Internal Revenue proposed a deficiency in tax on the ground that the gains from such sales were taxable at ordinary income rates. Pursuant to Section 272 of the Internal Revenue Code of 1939, petitioner filed a petition in the Tax Court of the United States for a redetermination of the deficiency proposed by the Commissioner. The Tax Court decided the case in favor of the Commissioner. After payment of the full amount of tax alleged to be due, petitioner filed a petition for review by the United States Court of Appeals for the Third Circuit. The Court of Appeals affirmed the decision of the Tax Court.

The sole issue is whether the Court of Appeals was correct in holding that the gains realized by Canton were gains on sales of real estate held by Canton primarily for sale to customers in the ordinary course of a real estate

business and were therefore taxable at ordinary income rates.

B. Facts.

The essential facts of this case may be summarized as follows:

During the taxable years, petitioner owned 99.875% of Canton's outstanding capital stock, and Canton in turn owned 100% of Canton Railroad's outstanding stock and 98.6% of Cottman's outstanding stock (R. 62a).

Canton Railroad is a Class 1 switching railroad which performs switching services between the industries located on its right of way, the Baltimore waterfront, and the three trunk lines servicing the City. Cottman is a stevedoring company which performs stevedoring operations for Canton Railroad and other companies. It leases from Canton and Canton Railroad an ore pier, cranes, a conveyor system, and all the facilities used by it in the unloading of ore from ships. Canton presently has invested in such facilities from four to five million dollars (R. 64a, 66a).

The real estate sales, the taxability of which is at issue in this case, were made by Canton. Almost all of such real estate was acquired by Canton immediately following its incorporation over one hundred years ago (R. 10a-15a).

Canton was incorporated in 1828 by a Special Act of the Maryland Legislature.[4] Shortly following its organization, it acquired over 5,000 acres of waterfront real estate in and near Baltimore. It thereafter began to lease portions of such real estate, making industrial improvements where the tenants so desired, and to construct waterfront facilities such as docks, wharves and piers. Some, if

4. Its charter provided, *inter alia*, that it is "capable in law of purchasing, holding, improving and disposing of property, real, personal or mixed . . . for the purposes herein authorized . . . and generally may do every other act or thing necessary to carry into effect the provisions of this Act, and promote the objects and designs of said company".

not all, the improvements then made were with a view to the continued holding and use of the property improved (R. 63a-64a). On a portion of Canton's property the United States Government constructed three or four warehouses during World War I. These buildings (which have a floor space of some 745,000 square feet) were subsequently acquired by Canton, and since that time the warehouse space has been leased for manufacturing and storage purposes (R. 66a).

In 1866, in order to furnish railroad facilities for its industrial and waterfront properties, Canton formed the Union Railroad, which was later sold to Pennsylvania Railroad interests. In 1906 Canton formed Canton Railroad as a connecting line between Baltimore's waterfront facilities and the trunk lines owned by the Baltimore & Ohio, Pennsylvania and Western Maryland Railroads (R. 64a).

Canton has been vitally interested in the development of the port of Baltimore. Efforts have been directed at improving and developing some of its waterfront property for continued use in its operations, while at the same time liquidating other portions. Additionally, the interests of Canton Railroad have been a strong influence on Canton's activities. Since the Railroad's construction, Canton has made it a policy to sell property suitable for industrial use only to purchasers who would increase traffic of the Railroad. Land not suitable for such purposes due to inaccessability has not been so restricted, and a large percentage has been sold for residential purposes (R. 67a).

Over the years Canton has gradually and continuously liquidated the portion of the original real estate investment not held for permanent rental or used in the railroad and stevedoring businesses of its subsidiaries, and has reinvested the sales proceeds therefrom (to the extent not distributed to its shareholders) in depreciable assets and industrial improvements for rental. For example, Canton's net depreciable assets increased by roughly 50% from January 1, 1950 to December 31, 1952 (R. 77a). By

1930 it had converted over 3,000 acres, and by the end of 1950, the first of the taxable years in question, its holdings were reduced to 887 acres (R. 68a).

During the ten years preceding the taxable years, Canton sold about eleven parcels a year (R. 72a). During the three taxable years it sold thirty-three parcels (aggregating roughly 105 acres) and realized a profit for purposes of Federal income tax with respect to twenty-two of them (R. 73a).[5]

After the major acquisition of real estate early in the nineteenth century, Canton made no purchases of real estate except for the purpose of straightening the boundary lines of its holdings or as right of way for a proposed extension of Canton Railroad in 1912 (R. 30a-32a, 64a-65a). In general, the real estate acquired to straighten boundary lines was purchased because it was thought that the various areas affected would be more attractive to industrial concerns which would be served by the Railroad (R. 49a-54a, 65a). The proposed extension was abandoned in 1925, and Canton's board of directors authorized Canton's president, at his discretion, to dispose of the real estate which had been acquired (R. 65a-66a).

Canton did not list its property with brokers, nor did it employ real estate brokers or agents (R. 68a). All its sales were handled by one officer, who devoted about a week a year to that activity (R. 76a). The prices were fixed by that officer, subject to approval by Canton's board of directors, and were comparable to what other sellers of similar property were receiving. Canton never personally solicited prospective buyers. All negotiations were initiated by the prospective purchasers or their brokers, and there was rarely any bargaining (R. 33a, 68a, 76a).

Although no "For Sale" signs were posted by Canton, it did, on occasion, prepare and make available brochures and maps describing its operations and real estate. It also

5. With respect to the other eleven parcels Canton realized a book profit, but no gain or loss for the tax purposes because the sale price was less than March 1, 1913 value and higher than provable cost.

advertised locally, from time to time, in magazines, newspapers and telephone directories (R. 69a-71a). This advertising related principally to real estate held for industrial purposes, and the cost thereof aggregated an average of less than one-tenth of one per cent of Canton's gross income during the taxable years (R. 17a-27a).

Since 1940 Canton has made no improvements except to real estate leased to third parties. Its only activities which might be termed a subdivision consisted of some grading and laying out a few streets, and was performed in the early 1900's with respect to real estate sold prior to 1940, more than ten years before the first taxable year in question (R. 48a-49a).

Canton's income is derived almost entirely from rentals, and its business activities consist of managing its rental properties (such as the Colgate Warehouses) and managing or supervising its subsidiaries. During the taxable years, the percentage of its gross income represented by rentals averaged almost 80%, three-fourths of which was attributable to leased real estate (R. 16a). Canton's other sources of income are interest, dividends and proceeds from the sale of real estate. The latter source, however, is relatively insubstantial, the profit therefrom averaging less than 7% of Canton's gross income during the taxable years, and in 1950 was only 1.25% (R. 5a, 11a-15a).

C. Decisions of the Courts Below.

On the basis of the foregoing facts, the Tax Court held that "Canton was engaged in the business of selling real estate to customers" (R. 79a). It so held notwithstanding it found (R. 79a) that Canton:

> ". . . owned most of the land sold during the taxable years for the more than one hundred years of its existence, that it did or did not in the interim make numerous other acquisitions of real estate, that when compared with its other operations its selling of real

estate and the profits therefrom were relatively small, or that in its organization and its methods of operation it was and is not the counterpart of the usual real estate development or brokerage business."

The Court of Appeals noted that Canton was liquidating a real estate investment. However, this fact played little part in the Court's decision. It affirmed the Tax Court's decision that Canton was in the real estate business solely because Canton made many sales and engaged in activities intended to make the liquidation profitable. More specifically (*infra*, Appendix B, page 34), the Court of Appeals apparently based its opinion upon evidence in the record relative to:

(a) Canton's advertising so as to reach prospective buyers;

(b) Its purchases to straighten boundary lines or shape up parcels;

(c) The continuity and regularity of its sales; and

(d) Its development of facilities to service industrial establishments it desired to attract to its property held for sale to industries.

It concluded (*infra*, Appendix B, page 36) that Canton's activities "were carried forward with such purpose, system and continuity . . . that the sales were to customers in the ordinary course of its business".

REASONS FOR GRANTING THE WRIT.

1. This Case Presents an Important Federal Question Which Has Caused Confusion in the Various Courts of Appeals and Has Not Been, But Should Be, Settled by This Court.

This case presents the question whether the real estate sold by Canton during the taxable years in question was held by it "primarily for sale to customers in the ordinary course of [its] trade or business" within the meaning of Section 117(a)(1)(A) of the Internal Revenue Code of 1939. If so (*i.e.*, if Canton was in the real estate business), the gains from such sales are taxable to Canton at ordinary income, rather than capital gains, rates.

The identical legal issue presented here has been raised in literally hundreds of cases before the lower courts,[6] and before nine Courts of Appeals,[7] but this Court has not yet considered it.

As the result of this vast amount of litigation, the lower courts have evolved numerous tests (for example, the extent of subdivision; the relation of real estate sales income to other income)[8] to be applied to the facts of a case

6. Research reveals at least 218 cases in the various lower courts deciding whether a taxpayer's real estate was held primarily for sale to customers in the ordinary course of his business.

7. *E.g.*, *Phipps v. Commissioner*, 54 F. 2d 469 (2d Cir. 1931); *Curtis Co. v. Commissioner*, 232 F. 2d 167 (3d Cir. 1956); *Lukin v. Commissioner*, 249 F. 2d 781 (4th Cir. 1957); *Alabama Mineral Land Co. v. Commissioner*, 250 F. 2d 870 (5th Cir. 1957); *Yunker v. Commissioner*, 256 F. 2d 130 (6th Cir. 1958); *Chandler v. United States*, 226 F. 2d 403 (7th Cir. 1955); *Dillon v. Commissioner*, 213 F. 2d 218 (8th Cir. 1954); *Palos Verdes Corp. v. United States*, 201 F. 2d 256 (9th Cir. 1952); *Home Co. Inc. v. Commissioner*, 212 F. 2d 637 (10th Cir. 1954).

8. In *Berberovich v. Menninger*, 147 F. Supp. 390 (E. D. Mich. 1957), the Court listed the following criteria: the frequency, continuity and activity in connection with the sales; the purpose for which the property was acquired and the motive in selling; the extent to which improvements were made in the act of subdividing; the extent to

to determine whether the taxpayer is in the real estate business. In the case of the person who from time to time sells real estate and re-invests in more, these tests are easily applied. The question is a simple, factual one: has he engaged in activities common to the typical real estate dealer?

Where, however, as in the present case, the taxpayer is gradually converting large acreage into cash or other business assets and does not replenish his holding through additional purchases, the views of the various Courts of Appeals differ substantially. The core of the dispute is whether the traditional tests nevertheless apply in such circumstances (as the Court of Appeals held here), or whether taxpayers who are liquidating capital assets may do so at capital gains rates if they are merely engaging in the minimum activities necessary to convert the assets to other investments. The resulting confusion in the administration of the internal revenue laws urgently requires resolution by this Court.

The problem is dramatically illustrated by the facts of this case. Approximately 90% of the real estate sold by Canton during the taxable years in question was acquired in whole or in part over one hundred years ago in an original acquisition of more than 5,000 acres. The obvious purpose for this acquisition was to capitalize upon the soaring land values which the handful of Canton's incorporators anticipated would result from Baltimore's growth in size and importance. Their aim was no different from any individual who invests in land in the outskirts of a modern city with the expectation that it will increase in value as the city expands. As Judge Augustus Hand said in *Phipps v. Commissioner*, 54 F. 2d 469, 471 (2d Cir. 1931):

> "Persons with large incomes of course invest their surplus funds in something, and if, to diversify their

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which the subdivision was advertised; the relation of the sales income to the taxpayer's yearly income; the extent of the business carried on; the length of time for which the property was held; and whether the taxpayer retained a broker.

holdings, they buy land, with the expectation of selling it when a good price is offered, such an expectation cannot, in our opinion, convert some sales of land that had been held for seven or eight years into a trade or business in real estate."

Following its incorporation and in later years, Canton made extensive improvements to portions of its investment, with a view to the continued holding and use of the property improved. It also developed, through subsidiary companies, substantial railroad and stevedoring businesses from which, in conjunction with its land and equipment rentals, it now realizes almost 90% of its income. The sales in question here were part of a gradual liquidation of the balance of the investment, which has continued for more than a century and by the close of the taxable years in question was still uncompleted. No further purchases of real estate were made except to round out portions of the initial investment, and except for one group of parcels acquired in connection with a proposed right of way for Canton Railroad. Upon abandonment of the right of way, the parcels acquired therefor have been liquidated in the same fashion as the original acquisition. The sales proceeds were re-invested in depreciable assets or industrial improvements for rental. During the course of the liquidation Canton carried on almost none of the typical activities normally associated with a real estate business. It did virtually no subdividing or advertising, employed no broker, never personally solicited purchasers, and had no real estate office.

The Tax Court held that Canton was a real estate dealer, despite the fact that "in its organization and its methods of operation it was and is not the counterpart of the usual real estate development or brokerage business" (R. 79a). The Court of Appeals affirmed this decision because, to paraphrase its reasons, Canton did some advertising to reach possible buyers; it rounded out portions of its initial investment; it developed facilities which served sites suitable for sale to industrial concerns; and there were

many sales in the course of the liquidation (*infra*, Appendix B, page 34). It considered that because Canton liquidated its holdings with "purpose, system and continuity", it was in the real estate business (*infra*, Appendix B, page 36).

The facts of this case thus squarely present an important question affecting an untold number of persons and corporations who invest incidentally in real estate for long-term gain: May they later liquidate their investment, using the minimum amount of business activity necessary to realize their whole expected profit, without being considered dealers in real estate for Federal tax purposes? As will hereinafter appear, this is a question with respect to which the various Courts of Appeals are in complete disaccord.

A. *There Is Confusion Among the Various Courts of Appeals With Respect to the Proper Tax Treatment of Real Estate Liquidations.*

The decision of the Court of Appeals in this case compounded the already existing confusion among the Circuits as to the proper tax treatment of the proceeds from a real estate liquidation. The varying approaches may be illustrated by reference to the following cases.

The Court of Appeals below relied heavily upon the fact that Canton's sales were frequent and continuous. This theory has been "pushed to extreme lengths in the Ninth Circuit". *United States v. Robinson*, 129 F. 2d 297, 300 (5th Cir. 1942). The Ninth Circuit at one time held that where the liquidation sales are frequent and continuous it follows almost necessarily that the taxpayer is in the real estate business. *Ehrman v. Commissioner*, 120 F. 2d 607, *cert. denied*, 314 U. S. 668 (1941). More recently, it has relaxed its position somewhat and now looks to the other traditional tests as well. It continues to hold, however, that these criteria are equally applicable to liquidations. In *Palos Verdes Corp. v. United States*, 201 F. 2d 256 (9th Cir. 1952), the Court conceded that the taxpayer

had purchased the property for investment many years previously and that his activities (including subdivision) in liquidating it were the only practicable means of disposal. The Ninth Circuit held that the taxpayer was nonetheless in the real estate business, saying (201 F. 2d at 258-9):

> "We have heretofore decided that a mere series of sales for the primary purpose of liquidation does not solve the problem. Ehrman v. Commissioner, supra. The holder may well have acquired and held the property for an ordinary turnover profit and found that it could not be sold for a reasonable price without submitting it to conditions prevalent to a trade or business. In such case the owner has changed the status of his holding, whether or not it was contrary to his first desire.
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> * * *
>
> "The evidence indicates to us that the owner was not in the real estate business by choice, but because it offered the way to dispose of the property which, to use an old expression, 'was eating its head off' through expenses of holding it. The owner did, however, resort to a method of disposal which in fact required that the property be submitted to customers in the ordinary course of trade or business of real estate."

In its most recent decisions in this area the Ninth Circuit reiterated this view. *E.g., Pool v. Commissioner*, 251 F. 2d 233 (1957), *cert. denied*, 356 U. S. 938 (1958).[9]

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9. In *McGah v. Commissioner*, 210 F. 2d 769 (9th Cir. 1954), the Ninth Circuit, under wholly different and unique circumstances, held that the sales there made were entitled to capital gains treatment. The taxpayers sold off a portion of their rental properties upon the demand of their bank that they reduce their indebtedness. The entire liquidation lasted less than three years. The Court properly concluded that since the decision to sell was involuntary the properties were not held primarily for sale to customers.

Thus the Ninth Circuit holds that where a taxpayer converting a capital investment in real estate to another investment is forced to break it up and sell in a business-like fashion, he must be deemed to have in fact entered the real estate business; what was theretofore a capital asset is transformed to stock in trade. That the taxpayer may not otherwise be able to capitalize upon his investment is, in the opinion of the Ninth Circuit, unimportant.

The Court of Appeals for the Seventh Circuit, on the other hand, recognizes economic reality. Under its view, a taxpayer converting land from a capital asset to cash must not be penalized merely because he engages in the minimum business activities necessary to realize the most profit from his investment.

In *Three States Lumber Company v. Commissioner*, 158 F. 2d 61 (7th Cir. 1946), a taxpayer liquidated a real estate holding of about 17,000 acres of timber land after it had removed the timber. The liquidation extended over more than thirteen years, during which period the taxpayer employed a person to devote full time to the sales. It also employed two full-time assistants to that man to handle the bookkeeping and show prospective buyers about the property. It did some advertising and also surveyed the tracts where necessary. It frequently loaned money for equipment and planting to people who had contracted for lease or sale of parcels. It held the land out for sale to persons who cared to purchase any amount of land consisting of ten or more acres. Some of the land was leased with an option to purchase, much of the land was sold under installment contracts. The Tax Court held that the sales were made in the ordinary course of the taxpayer's business:

> "The sale of its lands was, in a sense, a process of liquidation but it was carried on in such a way as to constitute a business. . . . It does not make any difference in this connection that the taxpayer's motive in selling the property is to liquidate his investment." 4 TCM 955, 956 (1945).

The Seventh Circuit, however, reversed the Tax Court and held that since the sales were no more than an orderly liquidation, the gains therefrom were capital gains.

More recently, in *Chandler v. United States*, 226 F. 2d 403 (7th Cir. 1955), the Seventh Circuit reversed the District Court and held that a taxpayer who (as part of the liquidation of over 1,000,000 acres) sold 290,000 acres in 536 sales over a nine-year period was entitled to treat the gains from the sales as capital gains. The Seventh Circuit said (at page 406):

> "Had the lands been sold in a single unit there probably would have been slight debate concerning their capital asset status. But the market place is hardly glutted with prospective buyers clamoring for million acre tracts. It seems odd to penalize this taxpayer because it actively sought to dispose of these holdings. Defendant would insist that Capitol sit idle, wishing for a buyer or buyers, under the threat that any selling effort would result in deprivation of capital asset treatment. Despite the blurring, in relevant precedent, between capital gain and ordinary income we think the specific facts established in this case warrant capital gain treatment for taxpayer's transactions."

The Sixth Circuit appears to follow the view of the Seventh. In *Yunker v. Commissioner*, 256 F. 2d 130 (6th Cir. 1958), where the taxpayer had liquidated through subdivision by a dealer and had also done some advertising, the Sixth Circuit said (at page 136):

> "If petitioner had sold the entire tract at a profit, in one transaction, it is unquestioned that she would be entitled to capital gains treatment. It was impossible for her to sell the entire tract at one time at a profit. To hold that she would not be entitled to capital gains treatment, when she would otherwise be entitled to it, merely because she selected the only possible method of selling her property at a profit, by installing im-

> provements and selling in smaller parcels, would seem to be an injustice resulting from a forced and artificial construction of the statute, which, in our view, could not have been intended by Congress."

The Eighth Circuit may also agree with the Seventh. Compare *Dillon v. Commissioner*, 213 F. 2d 218 (1954), where the Eighth Circuit said (at page 220):

> ". . . The [Tax] Court arrives at its conclusion on this point by a consideration of the business done in the taxable year 1946, and attaches no significance to the resolution of the taxpayer to liquidate his holdings in the houses in the fall of 1945. . . . We think the principle applied is neither legal nor reasonable, but that it is clearly erroneous."

The Fourth Circuit probably follows the Ninth. Compare *Oliver v. Commissioner*, 138 F. 2d 910 (4th Cir. 1943). The Fifth Circuit, although it recognizes that liquidation is a factor to be considered, tends to hold that it must be entirely passive and that the taxpayer may therefore engage in no selling activity whatever. *Alabama Mineral Land Company v. Commissioner*, 250 F. 2d 870 (5th Cir. 1957). But see *Riedel v. Commissioner*, 261 F. 2d 371 (5th Cir. 1958). The same might be said for the Tenth Circuit. Compare *Home Co., Inc. v. Commissioner*, 212 F. 2d 637 (10th Cir. 1954); *Maublin v. Commissioner*, 195 F. 2d 714 (10th Cir. 1952). And compare *Victory Housing No. 2, Inc. v. Commissioner*, 205 F. 2d 371 (10th Cir. 1953), where the Tenth Circuit held that gains realized by a corporation on the liquidation of a portion of its rental properties not considered essential to the continuation of its rental business were capital gains.[10]

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10. Although real estate cases have been before the Second Circuit, we do not believe that the facts of such cases are sufficiently similar to the present case to permit comparison. An earlier case would indicate that the Second Circuit follows the Seventh and would decide this case in favor of the petitioner. *Phipps v. Commissioner*,

It is difficult to say where the Third Circuit aligns itself within this welter of conflicting authority. Since it looked solely to the question of business activity and relied heavily on the Ninth Circuit's decision in *Stockton Harbor Industrial Company v. Commissioner*,[11] its decision appears to follow the reasoning of those Circuits holding that where there is some business activity and many sales, the liquidation must be a real estate business. However, the Third Circuit had earlier stated in *Curtis Company v. Commissioner*, 232 F. 2d 167 (1956), where the taxpayer was liquidating rental properties (at page 170):

> "We think it a case of one having an investment property on hand which he wants to turn into another form of investment. By the very nature of the case he had to sell the properties a piece at a time. Surely that does not make him a 'dealer' in these parcels of land any more than it would make a man a dealer if he wanted to liquidate his holdings in a corporate stock for which the market was weak so that he had to sell by small parcels instead of by one sale. That is the taxpayer's situation here."

In its opinion in this case the Court of Appeals sought to distinguish its earlier decision in the *Curtis* case on the ground that there the taxpayer had changed the purpose for which the property was held from rental to liquidation. This is quickly answered. If a taxpayer is liquidating, his aims in prior years are irrelevant. Indeed, he may, as here, have had no motive other than investment. The Court must look only to the taxpayer's situation when the liquidation began and the sales were made.

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54 F. 2d 469 (2d Cir. 1931) (sales proceeds held capital gains). However, in view of the recent multitude of cases in other circuits, it cannot be said that the Second Circuit would necessarily follow its earlier decision.

11. 216 F. 2d 638 (9th Cir. 1954), *cert. denied*, 349 U. S. 904 (1955).

The *Curtis* case is not only evidence of the conflict within the Third Circuit's own decisions, but also illustrates the divergent views of the various circuits. In the majority opinion rendered in the *Curtis* case, Judge Goodrich, after stating that the decisions of the circuits "indicate some disagreement not unnaturally", and that *Curtis* was "in the pattern which the majority of the Courts of Appeals have followed", thought that "Perhaps the Tenth Circuit would disagree with our decision".[12] On the other hand, the Ninth Circuit in its recent decision in the *Pool* case called attention to the "seemingly contrary conclusion" reached by the Third Circuit in the *Curtis* case, but noted that Judge McLaughlin's dissent in *Curtis* relied upon Ninth Circuit decisions.[13]

One final example of the confusion among the lower courts is worthy of mention. In a recent decision, reviewed by the full Court, the Tax Court held that the taxpayer there involved was engaged in the real estate business. *Longfellow v. Commissioner,* 31 T. C. No. 2 (1958). Judge Pierce, relying on decisions in the Second, Fifth, Sixth and Seventh Circuits, the Court of Claims, and various district courts, dissented on the ground that the sales were an orderly liquidation.[14] Ironically, Judge Pierce was the trial judge, the only member of the Court who had seen and heard the witnesses.

It must surely appear from the foregoing that review by this Court of this murky and troublesome question is direly needed.

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12. 232 F. 2d 167, 170 n. 9 (3d Cir. 1956).

13. 251 F. 2d 233, 236 n. 6 (9th Cir. 1957).

14. Compare *Altizer Coal Land Co. v. Commissioner,* 31 T. C. No. 10 (1958), where the Tax Court, noting that the real estate "could not be liquidated in any other manner than the method adopted without great financial sacrifice," held that the taxpayer was engaged in an orderly liquidation and was not in the real estate business.

B. The Decision of the Court of Appeals Below is Erroneous.

Needless to say, we vigorously dispute the holding of the court below that Canton was in the real estate "business". Indeed, the Tax Court found that its activities in no way resembled those of the typical dealer.[15] Furthermore, the approach of the Court of Appeals was to examine and discard individually the facts relied upon by the petitioner. In doing so, the Court failed to recognize the true over-all picture.

However, this Petition does not attack the right of the Court of Appeals to draw inferences from the facts, if its legal premise is correct. On the contrary, it is our position that the Court of Appeals erred in its view of the law; that its view is contrary to that of the Seventh, and other, Circuits; and that this Court should review the proceeding to rectify the error of the Third Circuit and clarify the issue for the benefit of all the lower courts.

The effect of the decision of the Court of Appeals is that no taxpayer may capitalize upon a large investment in real estate in a normal business fashion without being characterized a real estate dealer. The Court's decision is both economically unrealistic and contrary to the intent of the capital gains provisions of the internal revenue laws to permit investors to convert one investment to another without the penalty of ordinary income tax rates upon the profit built up over the years of the holding period.[16]

We hold with the view of the Seventh Circuit that Canton was not required to "sit idle, wishing for a buyer or buyers, under the threat that any selling effort would result in deprivation of the capital asset treatment".[17]

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15. It is difficult to find a real estate business where, as in Canton's case, the sale of each individual parcel must be approved by the board of directors.

16. S. Rep. No. 275, 67th Cong., 1st Sess. 12 (1930).

17. *Chandler v. United States*, 226 F. 2d 403, 406 (7th Cir. 1955).

Canton's activities relied upon by the Court of Appeals, in holding that Canton must pay ordinary income tax upon its gains, were only the steps of an investor attempting to make its real estate known to prospective buyers and enhance its value for maximum profit. Canton advertised, but only to the limited extent necessary to insure that buyers were aware that the real estate was available for sale. It rounded out the investment to make it more attractive, just as a holder of 49% of the stock of a company may purchase an additional 2% to interest a buyer desiring voting control. The construction of railroad facilities for industrial properties served, in part, the same purpose, but was also an established business from which Canton realized substantial income. Indeed, like any prudent investor, and entirely unlike a dealer anxious to turn over his inventory, Canton refused to sell its industrial properties to other than industrial concerns.

That Canton made many sales during the course of the liquidation is wholly immaterial. "Of course, where there is much to sell, there must or may be many sales." *Smith v. Commissioner*, 232 F. 2d 142, 145 (5th Cir. 1956).

To say, as did the Court of Appeals, that Canton was in the real estate business because it sold real estate with "purpose, system and continuity"[18] begs the question. Certainly Canton intended to sell its real estate, and certainly it liquidated as steadily as was possible without sacrificing price. No corporation with a responsible board of directors would do otherwise.

The Court of Appeals below confined its attention to the "business" tests and paid only lip service to the fact that Canton was liquidating an investment in the most advantageous, practical fashion. We submit that this approach is arbitrary and meaningless when the taxpayer is not turning over real estate into real estate and thus restocking his inventory as it is depleted. Taxpayers must

18. *Infra*, Appendix B, page 36.

indeed invest their capital in real estate at their peril if they cannot aggressively resell except at ordinary income rates. This injustice is aggravated by the vague guides to which taxpayers must look if they wish to avoid the tax consequences which are said to follow if they engage in "business".

The Courts of Appeals disagree whether a taxpayer may liquidate a real estate investment using the minimum normal business means and yet retain the capital nature of the investment. The view of the Court of Appeals below—that he may not, if he is too business-like—is erroneous. Accordingly, we respectfully urge the Court to issue the writ of certiorari here sought and remove the confusion by reversing the judgment of the Third Circuit.

CONCLUSION.

For the foregoing reasons, it is submitted that this Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX A.

Internal Revenue Code of 1939.

§ 117. Capital Gains and Losses.

(a) **Definitions.**—As used in this chapter—

(1) **Capital Assets.**—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include—

(A) stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;

(B) property, used in his trade or business, of a character which is subject to the allowance for depreciation provided in section 23(l) or real property used in his trade or business;

(C) a copyright; a literary, musical, or artistic composition; or similar property; held by—

(i) a taxpayer whose personal efforts created such property, or

(ii) a taxpayer in whose hands the basis of such property is determined, for the purpose of determining gain from a sale or exchange, in whole or in part by reference to the basis of such property in the hands of the person whose personal efforts created such property; or

(D) an obligation of the United States or any of its possessions, or of a State or Territory, or any political subdivision thereof, or of the District of Columbia, issued on or after March 1, 1941, on a discount basis and payable without interest at a fixed maturity date not exceeding one year from the date of issue.

* * *

(4) **Long-Term Capital Gain.**—The term "long-term capital gain" means gain from the sale or exchange of a capital asset held for more than 6 months, if and to the extent such gain is taken into account in computing gross income;

* * *

(6) **Net Short-Term Capital Gain.**—The term "net short-term capital gain" means the excess of short-term capital gains for the taxable year over the short-term capital losses for such year;

* * *

(8) **Net Long-Term Capital Gain.**—The term "net long-term capital gain" means the excess of long-term capital gains for the taxable year over the long-term capital losses for such year;

Treasury Regulations 111.

§ 29.117-1. **Meaning of terms.**—The term "capital assets" includes all classes of property not specifically excluded by section 117 (a) (1). In determining whether property is a "capital asset," the period for which held is immaterial.

The exclusion from the term "capital assets" of property used in the trade or business of a taxpayer of a character which is subject to the allowance for depreciation provided in section 23 (l) and of real property used in the trade or business of a taxpayer is limited to such property used by the taxpayer in the trade or business at the time

of the sale, exchange, or involuntary conversion. Gains and losses from the sale or exchange of such property are not subject to the percentage provisions of section 117 (b) and losses from such transactions are not subject to the limitations on losses provided in section 117 (d), except that under section 117 (j) the gains and losses from the sale or exchange of such property held for more than six months may be treated as gains and losses from the sale or exchange of capital assets, and may thus be subject to such limitations. See section 29.117-7. Property held for the production of income, but not used in a trade or business of the taxpayer, is not excluded from the term "capital assets" even though depreciation may have been allowed with respect to such property under section 23 (l) prior to its amendment by the Revenue Act of 1942. However, gain or loss upon the sale or exchange of land held by a taxpayer primarily for sale to customers in the ordinary course of his business, as in the case of a dealer in real estate, is not subject to the limitations of section 117 (b), (c), and (d). The term "ordinary net income" as used in these regulations for the purposes of section 117 means net income exclusive of gains and losses from the sale or exchange of capital assets.

Treasury Regulations 118.

§ 39.117 (a)-1. Meaning of terms. (a) The term "capital assets" includes all classes of property not specifically excluded by section 117 (a) (1). In determining whether property is a "capital asset," the period for which held is immaterial.

(b) The exclusion from the term "capital assets" of property used in the trade or business of a taxpayer of a character which is subject to the allowance for depreciation provided in section 23 (l) and of real property used in the trade or business of a taxpayer is limited to such property used by the taxpayer in the trade or business at the time

of the sale, exchange, or involuntary conversion. Gains and losses from the sale or exchange of such property are not treated as gains and losses from the sale or exchange of capital assets, except to the extent provided in section 117 (j). See § 39.117 (j)-1. Property held for the production of income, but not used in a trade or business of the taxpayer, is not excluded from the term "capital assets" even though depreciation may have been allowed with respect to such property under section 23 (l) before its amendment by section 121 (c) of the Revenue Act of 1942. However, gain or loss upon the sale or exchange of land held by a taxpayer primarily for sale to customers in the ordinary course of his business, as in the case of a dealer in real estate, is not subject to the provisions of section 117. The term "ordinary net income," as used in the regulations in this part for the purposes of section 117, means net income exclusive of gains and losses from the sale or exchange of capital assets.

APPENDIX B.

Opinion of the Court Below.

(Filed November 26, 1958)

Argued October 8, 1958

Before GOODRICH, MCLAUGHLIN and STALEY, *Circuit Judges.*

By STALEY, *Circuit Judge.*

The sole question presented by these appeals is whether gains realized by the taxpayer on the sale of real estate during the years 1950, 1951, and 1952 are taxable as long-term capital gains or as ordinary income.

The facts, which are set forth in some detail in the opinion of the Tax Court,[1] may be summarized as follows:

The Pennroad Corporation is an investment company registered with the Securities and Exchange Commission as a closed-end management company pursuant to the Investment Company Act of 1940. During the tax years in question, Pennroad, a Delaware corporation, as the common parent corporation of an affiliated group of companies, filed consolidated income tax returns for itself and its affiliates. Among these affiliates was the Canton Company of Baltimore (Canton), of which the taxpayer owned 99.875 per cent of the outstanding capital stock. In turn, Canton owned 100 per cent of the stock of the Canton Railroad Company and 98.6 per cent of the stock of The Cottman Company.

The real estate sales, the taxability of gains from which are at issue, were made by Canton. Canton was incorporated in 1828 by a Special Act of the Maryland Legislature. Its charter provides that it is "capable in law of

1. 29 T. C. — (1958) (No. 98).

purchasing, holding, improving and disposing of property, real, personal or mixed . . . for the purposes herein authorized . . . and generally may do every other act or thing necessary to carry into effect the provisions of this act, and promote the objects and designs of said company." The purposes for which Canton was incorporated are set out in the margin.[2]

The Canton Railroad, for which Canton procured a charter in 1906, is presently a Class 1 switching railroad under Part I, Section 20 of the Interstate Commerce Act. It performs switching services between the industries located on its right of way, the Baltimore waterfront, and the three trunk lines servicing the city. The Cottman Company is a stevedoring company, control of which was acquired by Canton on July 19, 1950. It performs stevedoring operations for the Canton Railroad and other companies and leases from Canton and Canton Railroad an ore pier, cranes, a conveyor system, and all of the facilities utilized by it in the loading and unloading of ships.

Shortly following its organization in 1828, Canton acquired over 5,000 acres of waterfront real estate in and

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2. "* * * [T]he improvement . . . of any lands and appurtenances which shall belong to the said company, by laying out into lots, streets, squares, lanes, alleys, and other divisions, any such lands within the vicinity of the city of Baltimore, or near to any navigable water, and erecting, constructing, or making thereon all such wharves, ships, boats and other vessels, workshops, factories, warehouses, stores, dwellings, and such other buildings and improvements as may be found or deemed necessary, ornamental or convenient; and letting, renting, leasing, selling or granting, on conditions, or using any lot or other portion of any of the said lands for agricultural, mining or manufacturing purposes, or any wharf, house, or other building or improvement, to be used by any mechanic or artisan, or other person, whether in the employ of the said company or not, in carrying on any lawful trade, business, or manufacture, authorized or permitted by the laws of this State. Provided that in laying off streets, squares, lanes, alleys or other divisions no infringement be made on the plan of the city of Baltimore, as laid out by the Commissioners under the act passed at December Session 1816 Chapter 209. And Provided also, that the said company and its agents shall in all cases whatsoever be subject to and observe the ordinances of the City of Baltimore within the limits of said City."

near Baltimore, Maryland. It thereafter leased, improved, and sold portions of this real estate. In addition, it constructed waterfront facilities, such as docks, wharves, and piers. The parties agree that some, if not all, of the improvements then made were with a view to the continued holding and use of the property improved. On a portion of Canton's property the United States government constructed three or four warehouses during World War I. These buildings were subsequently acquired by Canton and since that time one of its activities has been the leasing of warehouse space for manufacturing and storage purposes.

Over the years, Canton purchased additional parcels of real estate. Some of these purchases were effected in anticipation of a proposed extension to the Canton Railroad, which plan was later abandoned. A number of parcels so acquired were purchased because they were regarded as having strategic locations along the proposed route, such as at highway intersections. Other acquisitions were made periodically for the avowed purpose of filling out or shaping up irregular parcels already held by Canton, so as to make them more attractive to persons in the market for industrial sites.

In keeping with its purposes as set forth in its charter, Canton has been vitally interested in the development of the Port of Baltimore. Efforts have been directed at improving and developing its waterfront property for continued use in its operations, while at the same time selling or marketing other portions of its real estate. Additionally, the interests of the Canton Railroad have been a strong influence on Canton's activities. Since the railroad's construction, Canton has made it a policy to sell property suitable for industrial use to purchasers who would increase the traffic of the railroad. Land not suitable for such purposes due to inaccessability has not been so restricted, and a large percentage has been sold for residential purposes.

By 1930 Canton retained approximately 1,700 acres of real estate, the rest having been liquidated. Subsequently,

it sold real estate at a reasonably steady rate up to and including the taxable years. Canton did not list its property with brokers nor did it employ agents or brokers to dispose of its property. The prices for property were fixed by one of its officers subject to approval by its board of directors, such prices being comparable to what other sellers of similar property were receiving.

Although no "For Sale" signs were posted by Canton, it did, from time to time, prepare and issue brochures and maps describing its operations and available real estate. It also advertised locally in magazines, newspapers, and telephone directories. Rather consistently Canton described itself as dealing in "Industrial Real Estate." At times it also indicated that it had large or small tracts available to builders for residential purposes.

During the tax years in question, 1950, 1951, and 1952, thirty-three sales were consummated for an income tax profit of $293,949.19.[3] A substantial number of the parcels were from the original acquisition of 5,000 acres; others were acquired as part of the plan to extend the Canton Railroad, and still others or portions thereof were acquired for the purpose of "straightening boundary lines." With the exception of two parcels, all of the land was unimproved and only one-third of the parcels had been rented at any time during the preceding ten years, most of them for outdoor advertising or farming operations at nominal rentals.

For federal income tax purposes, Canton always treated gains from the sales of its real estate as capital gains, and this was not questioned by the government until 1949. Taxpayer's consolidated returns for the tax years

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3. Canton realized a book profit on each of the 33 sales made during the taxable years, but on eleven of the 33 it realized no gain for income tax purposes. Each of the eleven sales on which no income tax gain was realized was of land acquired in 1834, or prior thereto, and presumably the differences between book profit and gain for income tax purposes were due primarily to differences between March 1, 1913, fair market value and cost or some other book basis.

in question described Canton's business as "Real Estate—Active." During 1940-1950 the taxpayer stated in its annual reports to its stockholders that "Canton Company of Baltimore was chartered in Maryland in 1829 [sic] for the purpose of dealing in real estate, etc. The principal business is the sale and/or rental of real estate." Canton's annual reports for 1951 and 1952 referred to the land that had been sold as "unimproved land which had been held for many years as an investment." Its annual reports for the immediately preceding years contained no such statement.

The Tax Court found that "The real estate sold by Canton during the taxable years 1950, 1951 and 1952 was held by it primarily for sale to customers in the ordinary course of its business." It is this finding which taxpayer attacks here. Of course it is in the nature of an ultimate finding of fact and, since such finding is but a legal inference from other facts, this court has held that it is subject to review free of the restraining influence of the "clearly erroneous" rule applicable to ordinary findings of fact made by the trial court. Philber Equipment Corp. v. Commissioner of Internal Revenue, 237 F. 2d 129 (C. A. 3, 1956); Curtis Co. v. Commissioner of Internal Revenue, 232 F. 2d 167 (C. A. 3, 1956). However, where the ultimate fact reasonably flows from the basic facts and especially where the basic facts are persuasive of the ultimate fact so found, this court will not disturb the finding of the trial court. Commissioner of Internal Revenue v. Scottish American Investment Co., 323 U. S. 119 (1944); McKelvey v. Commissioner of Internal Revenue, 246 F. 2d 609 (C. A. 3, 1957). The present case meets this standard.

Taxpayer characterizes Canton's activities as evidencing a gradual, passive liquidation of its original real estate holdings purchased over one hundred years ago. It concludes that the real estate Canton sold during the tax years was either a capital asset under Section 117(a), or prop-

erty used by it in its trade or business under Section 117(j) of the Internal Revenue Code of 1939.[4]

That property is being liquidated does not foreclose the question, for as was said in Home Co., Inc. v. Commissioner of Internal Revenue, 212 F. 2d 637, 641 (C. A. 10, 1954):

> "One may, of course, liquidate a capital asset. To do so it is necessary to sell. The sale may be conducted in the most advantageous manner to the seller and he will not lose the benefits of the capital gain provision of the statute, unless he enters the real estate business and carries on the sale in the manner in which such a business is ordinarily conducted. In that event, the liquidation constitutes a business and sale in the ordinary course of such a business and the preferred tax status is lost."

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4. "§ 117. Capital gains and losses

"(a) Definitions. As used in this chapter—

"(1) Capital assets. The term 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include—

"(A) stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business;

"(B) property, used in his trade or business, of a character which is subject to the allowance for depreciation provided in Section 23(*l*), or real property used in his trade or business;

* * *

"(j) Gains and losses from involuntary conversion and from the sale or exchange of certain property used in the trade or business.

"(1) Definition of property used in the trade or business. For the purposes of this subsection, the term 'property used in the trade or business' means property used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23(*l*), held for more than 6 months, and real property used in the trade or business, held for more than 6 months, which is not (A) property of a kind which would properly be includible in the inventory of the taxpayer if on hand at the close of the taxable year, or (B) property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business * * *." 26 U. S. C. A. (I. R. C. 1939) § 117 (j).

During the tax years Canton invested the proceeds of the real estate sales in depreciable assets and not in new real estate. This is relied upon by the taxpayer as indicative of the purpose of its operations. In Curtis Co. v. Commissioner of Internal Revenue, 232 F. 2d 167 (C. A. 3, 1956), that fact was considered among others and led to the conclusion that as to property which had been developed by the Curtis Company as a housing rental business, a true liquidation was being carried forward, but as to the undeveloped parcels there had been no showing of a change in the purpose for which the property was being held—real estate sales. When considered as one of many factors present in this case, the reinvestment facts appear far from determinative. Canton still had considerable real estate for sale and had purchased irregular parcels in the recent past for the purpose of making it more attractive to purchasers. Canton showed no decisive evidence of intention to change the nature of its business or businesses and therefore the Curtis case is inapposite.

In considering Section 117, the Supreme Court has recently stated in Corn Products Refining Co. v. Commissioner of Internal Revenue, 350 U. S. 46, 52 (1955):

> "* * * Congress intended that profits and losses arising from the everyday operation of a business be considered as ordinary income or loss rather than capital gain or loss. The preferential treatment provided by § 117 applies to transactions in property which are not the normal source of business income. It was intended 'to relieve the taxpayer from * * * excessive tax burdens on gains resulting from a conversion of capital investments, and to remove the deterrent effect of those burdens on such conversions.' Burnet v. Harmel, 287 U.S., at 106. Since this section is an exception from the normal tax requirements of the Internal Revenue Code, the definition of a capital asset must be narrowly applied and its exclusions interpreted broadly. This is necessary to effectuate the basic congressional

purpose. This court has always construed narrowly the term 'capital assets' in § 117."

Canton not only acquired substantial holdings of real property at or shortly after its incorporation but added to these holdings in later years. The Tax Court was of the opinion that the purpose for which these properties were being held at the time of sale could be discerned from the evidence in the record relative to advertising so as to reach prospective buyers; the purchase of property so as to straighten boundary lines or shape up parcels; the continuity and regularity of sales; and the development of facilities by Canton so as to service industrial establishments it desired to attract to its property held for sale to industries.

The taxpayer's contention that its sales were not conducted in the ordinary course of business since it restricted sales, by and large, to purchasers who would in turn increase the traffic of the Canton Railroad has been adequately answered by the Tax Court. We find nothing in Section 117 which would indicate that sales to a somewhat restricted group of purchasers are not to be considered as sales to customers. The word is to be given its normal meaning and under these facts it is abundantly clear that Canton had "purchasers" or "buyers" for its real estate.

The fact that little, if any, subdividing was carried on by Canton was not considered significant by the Tax Court, and we feel rightly so. In view of the purpose for which it was being held—industrial development— the statement in Stockton Harbor Industrial Co. v. Commissioner of Internal Revenue, 216 F. 2d 638, 655-656 (C. A. 9, 1954), cert. denied, 349 U. S. 904 (1955), appears particularly apt:

> "The fact that no subdivision was attempted has no significance. While it is the practice in California and elsewhere to subdivide property held for residential purposes or for mixed residential and business purposes, large industrial sites may derive their chief value

from their availability in an undivided and unmapped tract. And it can be seen readily that it might be better business policy to keep a tract of over nine hundred acres, located on an island at Stockton Harbor, ready to satisfy the needs of large industrial plants and allow them to make their own selections, rather than relegate them to choosing from predetermined sites in a subdivided tract. Hence the failure to subdivide and break up the holdings is consistent with the purpose for which the property was held."

The Stockton case brings to the foreground a most important factor that the taxpayer appears to have overlooked. A number of so-called tests or aids in determining whether a business of selling real estate exists were developed in cases dealing with property devoted to residential purposes. Certainly the type and amount of advertising, subdivision, development, solicitation, holding period prior to sale, etc., are decidedly different when dealing with industrial property, as most of the property in the instant case has been characterized.

Two additional points raised by the taxpayer deserve some mention. It has been urged that Canton's income from the sale of real estate was small in comparison with its income from rentals and dividends. This is of little, if any, significance when it is recognized that a company may have more than one business or more than one aspect to its business. Williamson v. Commissioner of Internal Revenue, 201 F. 2d 564 (C. A. 4), cert. denied, 345 U. S. 970 (1953); Friend v. Commissioner of Internal Revenue, 198 F. 2d 285 (C. A. 10, 1952); Fackler v. Commissioner of Internal Revenue, 133 F. 2d 509 (C. A. 6, 1943). Inasmuch as Canton's sale of real estate was sizeable and not de minimis, we see no merit in this contention.

Lastly, the taxpayer, relying on Chandler v. United States, 226 F. 2d 403 (C. A. 7, 1955), submits that self-characterization by a party of its activities is not worthy of weight. In the Chandler case the court states at page 406:

> "* * * That taxpayer indicated in a 1942 protest to an Internal Revenue Agent [that] it was a dealer in real property is hardly determinative of the total appeal. Self-description, such as that in the setting of this case is well wide of the mark and but a speck on the periphery."

There the isolated statement to the Internal Revenue agent was rightly not determinative of the *total appeal*, for, as indicated, the setting of the case must be considered. In the instant case, we have self-characterization in the returns for all three years, similar statements in annual reports for the years 1940 through 1950, advertising of similar purport, and a state of facts that justifies reliance upon these descriptions by the taxpayer of its business. Pacific Homes, Inc. v. United States, 230 F. 2d 755 (C. A. 9, 1956); Wite v. Commissioner of Internal Revenue, 172 F. 2d 629 (C. A. 5, 1949).

Accordingly, since the activities of Canton, culminating in the sales in question, were carried forward with such purpose, system, and continuity, we are persuaded that the sales were to customers in the ordinary course of its business.

The decisions of the Tax Court will be affirmed.

Judgments of the Court Below.

No. 12,597.

Present: GOODRICH, MCLAUGHLIN and STALEY, *Circuit Judges.*

This cause came on to be heard on the record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged and decreed by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

Attest:

IDA O. CRESKOFF
Clerk

November 26, 1958

No. 12,598.

This cause came on to be heard on the record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged and decreed by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

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November 26, 1958